
BUDGET AND PERFORMANCE INTEGRATION

1. BUDGET AND PERFORMANCE INTEGRATION

This Budget marks a significant step on the long road to a results-oriented government. It starts using performance measures to develop policies, to make budget decisions, and to improve everyday program management. The Administration is creating a government that promotes the outcomes that Americans want—such as better education for our children, the freedom to travel safely, and protection of our health—and does this in a cost-effective and efficient way.

Achieving better program performance—particularly better performance for each dollar spent—is a high priority of this Administration. Congressional interest, reflected in the Government Performance and Results Act of 1993, set agencies to identifying performance goals, planning to achieve them, and reporting on results.

What has been missing is systematic use of these measures to make decisions. In particular, performance measures are not directly linked to the budget—and yet it is the budget that drives policy development, allocates resources, and has undeveloped potential to support better management.

- Past and planned results are not shown with budget requests, let alone linked in a cost-and-results relationship.
- Program managers responsible for achieving results often do not control the resources they use or have flexibility to use them efficiently.
- Performance and cost data are recorded in separate systems and not integrated to provide timely, analytical, feedback to decision-makers and managers.
- Americans cannot readily assess program results, and cannot compare performance and cost across programs.

Budgeting for Results. Eager to make government work better, the Administration used all of the performance information it could gather in making decisions for this Budget. It also began the transition to change the burden of proof, asking agencies and advocates to supply evidence of program effectiveness instead of assuming effectiveness in the absence of evidence to the contrary. In addition to funding high priority programs, the Budget devotes dollars to programs that are rated effective. The Budget proposes reforms for ineffective

programs, reduces their funding or terminates them. Policy changes are proposed to increase program effectiveness and to improve the efficiency of programs and support services. The first section of this chapter, Budgeting for Results, analyzes shifts in resources and changes in policies made on the basis of this intense focus on performance.

Foundation for Results. To create a foundation for continual improvement in the effectiveness of government, the President has begun to make results the focus of the budget process. Planning and evaluation will be integral to budgeting. The budget takes the first steps toward showing expected results and the resources requested to achieve each result. To give managers full information about programs and to encourage efficient use of resources, the budget needs a uniform measure of the full annual cost of the resources used that will be charged to each program and activity.

In October, the President transmitted to Congress the Managerial Flexibility Act of 2001. Title II of that Act will charge employing agencies for the full annual accruing cost of Federal pensions and retiree health benefits, as reflected in this Budget. The Administration is developing proposals to charge for support services, capital assets, and hazardous substances cleanup where these resources are used. As explained in the second section of this chapter, Foundation for Results, these proposals do not change total budget outlays, budget concepts, or public-private cost comparisons. However, they would provide a better assessment of program costs.

Managing for Results. Budget and Performance Integration is one of five interrelated initiatives in *The President's Management Agenda*, rolled out in August. The others are Strategic Management of Human Capital, Competitive Sourcing, Expanded Electronic Government, and Improved Financial Performance. The third section of this chapter, Managing for Results, shows that the objective of these five initiatives together is to create a transformation to year-round performance orientation through all levels of the Federal government.

“We are not alone...”

Governments here and around the world are devising strategies to assess and manage for results—both outputs (i.e., products and services delivered) and outcomes (i.e., the end result that is being sought, such as clean streets or reduced crime).

Here in the United States, a growing number of States, counties and municipalities use “performance budgeting” as a tool for making policy and management decisions. **Charlotte**, North Carolina, and **Dayton**, Ohio undertake regular performance measurement. **Sunnyvale**, California has become internationally recognized for performance budgeting—allocating funding for tasks rather than for personnel, equipment, and supplies, with quantified objectives that are expected to be achieved with the funding. **Indianapolis’** budget provides mission statements, allocations by outcome objectives, and comparative performance measures.

State governments are also using these tools. **Missouri**, **Texas**, **Louisiana** and **Virginia** use performance information extensively in the central budget office, while most States use performance information at the agency level.

Successful implementation of performance-based budgeting has not been limited to this country. Over the past two decades, every year an increasing number of the 30 countries in the Organization for Economic Cooperation and Development are adopting a performance-based approach to management. **New Zealand** focused on “buying outputs” ten years ago. **Australia** and the **United Kingdom** are the leaders in focusing on outcomes. **Canada** and the **Netherlands** are close behind, with **France** and **Japan** still in the early phases of transforming to an outcome-focused approach.

Australia develops effectiveness and efficiency outputs for its outcomes, and prices each output. The British system is more structured than Australia, employing performance service agreements, aim (or mission) statements, overarching objectives, performance targets, and statements of responsibility for delivery (achieving the targets). In linking resources with outcomes, the British Cabinet Committee’s annual budget review allocates monies three years forward, making decisions on both broad outcome levels and the resources needed to achieve the outcome levels.

BUDGETING FOR RESULTS

Testifying before Congress last May, the Director of OMB signaled his intention to focus on performance. “Our main focus of the next months will be working toward full integration of budget and performance information, and using performance data to help make program and budget decisions.” He described three specific steps in this direction.

- “First, we will insist that agencies develop a credible linkage between resources and performance. We need to be able to answer the question: ‘What are we getting for what we are spending?’ As we work to establish this linkage, we expect to make some changes to the traditional process of how we review budget requests, and the nature of our passback to the agencies on their requests.
- “Second, we intend to improve our ability to understand the true cost of each program. Full costing of certain program budget accounts will necessitate significant accounting changes, and we are developing a legislative proposal permitting us to assign currently unallocated costs and present these in the budget.
- “Third, you should see a more robust presentation of performance information in the FY 2003 President’s Budget. We also intend to explore how a significant restructuring of the budget document

itself might enhance public and Congressional understanding of government performance.”

“Work is already underway on these and several related initiatives. These tasks will engage nearly every OMB office, and will comprise a significant part of the workload over the next year.” The Director concluded: “We believe that this work will lead to a big potential payoff in improved effectiveness and efficiency of government.”

OMB staff and agencies collected evaluations, studies, and performance documentation of all sorts from all sources to assess which programs were effectively improving desired outcomes. Within the Executive Branch, preliminary assessments of these materials were discussed, and agencies were urged to improve program performance and to improve evidence of effectiveness and linkage with program cost.

Below are some of the results of this performance-oriented process of policy development and budget allocation. The examples illuminate ways in which policy makers and program managers can help government better serve its citizens. Deliberately, they are chosen to represent “best practice”—examples from which other program managers and policy makers can learn. They are presented in five categories: (1) funding effective programs, which have demonstrated benefits greater than cost; (2) shifting resources toward more effective

programs from less effective ones that have similar purposes; (3) setting program targets and strategies based on understanding performance and cost relationships; (4) adding incentives to enhance program effectiveness; and (5) improving efficiency in programs and support services.

Funding Effective Programs

Programs in this category are effective. They deliver real benefits for Americans—healthier babies and families, more disadvantaged youths off drugs and in school or job training, and advancing knowledge that can improve health and sustain economic growth. These programs have undergone evaluation, not only documenting their effectiveness, but developing understanding of the reasons for their success so that policy makers and program managers can sustain and build on it.

- **Agriculture:** Numerous government and private studies show that the Special Supplemental Nutrition Program for Women, Infants and Children (WIC) is one of the nation's most successful and cost-effective early intervention programs. The program saves lives and improves the health of women, infants and children who are nutritionally at risk. The Budget reflects this demonstrated success by fully funding the program in 2003 to enable all eligible persons who seek services to receive them. The request is sufficient to provide 7.8 million persons with supplemental foods, nutrition education, and preventive health care each month in 2003. A contingency fund is available to serve an expanded number should that be necessary.
- **Commerce:** Although the U.S. gross domestic product (GDP) statistics are widely regarded as among the best in the world, they require continual improvement to keep pace with the nation's rapidly changing economy. Additional funding is proposed for the Bureau of Economic Analysis to improve and speed production of its statistics, on which government and business decision-makers depend.
- **Health and Human Services:** Community Health Centers provide high-quality health care that reduces hospitalizations and emergency room use, and prevents expensive chronic disease and disability. The Budget expands the number of centers by 1,200 to serve an additional 6.1 million patients by 2006. Together with the National Health Service Corps, the Centers increase the number of health care providers in underserved areas.
- **Health and Human Services:** The 1997 National Treatment Improvement Evaluation Study found that treatment decreased primary drug use by 48 percent, alcohol and drug-related medical visits by 53 percent, and criminal activity by as much as 80 percent. Welfare dependency, and

homelessness also declined. The Budget supports an additional 52,000 drug treatment slots.

- **Health and Human Services:** Funding for the National Institutes of Health, the world's leading research institution for biomedical and behavioral research, will increase to double its 1998 level. NIH conducts research in its own laboratories, but the vast majority of its funding supports researchers in universities, hospitals, and research institutes around the country through peer-reviewed grants. NIH has supported great advances in the detection and treatment of disease, and its recent work on the human genome, cancer, and many other diseases gives promise of accelerating breakthroughs.
- **Labor:** The Budget will support four more Job Corps centers for residential vocational training for disadvantaged youth than in 2001. At a unit cost of roughly \$31,700 per service year, the Job Corps is the Department of Labor's costliest training program. However, evaluations have demonstrated that its benefits exceed its costs. Job Corps participants get jobs, keep them, and increase earnings over their lifetimes.
- **National Science Foundation:** The NSF, a leader among Federal agencies that fund basic research, will get more funding and programs transferred from other agencies. Of NSF's grants, 94 percent are competitive, based on merit review. Each year, one-third of NSF's research and educational programs are evaluated for integrity, efficiency, and quality of results, so that all programs are reviewed in a three-year period. Of the dozen 2001 Nobel prize winners in the sciences, NSF supported eight for the research that won them the award. NSF quickly redirects resources to areas of emerging opportunity, and invests one-quarter of its research budget in areas where major breakthroughs are likely.

Shifting Resources toward More Effective Programs

Comparison of programs for similar purposes can lead to the conclusion that some are more effective than others. Shifting resources toward the better programs is one way to improve results, while the other programs seek ways to focus or reform their efforts.

- **Commerce:** Funding for technology innovation in the Department of Commerce was increased for the National Institute of Standards and Technology, a world leader in high-tech and basic industrial standards including work that led to the 2001 Nobel Prize in physics. The Patent and Trademark Office will also have more resources and set targets for faster patent and trademark processing. The Budget channels resources to higher performing programs by reducing funding for Manufacturing Extension Partnerships and the Advanced Technology Program, and terminating the Technology Opportunities Program.

- **Housing and Urban Development:** Housing vouchers are lower in cost per unit, at only 85 percent of the cost of Public Housing, and benefits are higher. More voucher recipients (26 percent) than Public Housing dwellers (8 percent) live in census tracts with less than 10 percent poverty; evaluations are finding better educational, social and behavioral outcomes from the greater opportunities available in these neighborhoods. The Budget increases funding for housing vouchers, expands opportunities for families to choose housing that best fits their needs, and provides more help to see that vouchers are used effectively.
- **Labor/Training:** This Budget begins a wide-ranging reform of Federal investments in training and employment. In 2002, there are at least 48 overlapping training and employment programs scattered around 10 agencies. For several programs that are duplicative or have a history of poor performance, funding is reduced or terminated, reducing the number of programs from 48 to 28. For the many other training programs where performance measures are inadequate or not comparable, a multi-year effort will begin to assess relative effectiveness, shift resources to programs that prove effective, and eliminate ineffective or duplicative programs.
- **Labor:** The backlog of the H1-B visa program will be eliminated by shifting funds from an ineffective grant program, and reforming the visa review process.
- **Research:** Rigorous peer review of proposals for research is an effective tool in selecting projects that are most likely to yield useful results. The Budget more than doubles funding for USDA's National Research Initiative, and reduces other agricultural research, in an effort to increase peer review. Also to promote merit-based competition, NOAA's Sea Grant program, and the Interior Department's toxic substances hydrology program will move to NSF.
- **Corps of Engineers:** For the Corps navigation program, the Budget funds improvements for those waterways with the greatest economic return, and limits funding for those with little commercial traffic.

Setting Program Targets and Strategies

As programs learn to link performance and cost, they can set targets in their annual performance plan in line with their budget request. This helps to gain support for their request and holds them accountable to achieve the targets. Understanding relationships between cost and performance helps to achieve better performance, to gauge the additional cost of additional performance, and, in some programs, to set appropriate fees.

- **Commerce:** The National Weather Service, an effective program, got an increase in funding and specific targets to increase hurricane warning lead

time two hours by 2005, double tornado lead time to 22 minutes by 2015, improve aviation forecasting accuracy by 13 percentage points by 2007, and improve temperature and river forecasts for a pilot region by 2004. Lives will be saved by more timely evacuations; airline and energy industry costs and energy use will be reduced.

- **Health and Human Services:** The Food and Drug Administration plans to increase the speed of processing generic drug applications to act on 75 percent within six months of receipt in 2003, up from 50 percent in 2001. FDA will also triple inspections of foods it regulates that are imported into the United States.
- **Housing and Urban Development:** HUD has set a target to raise the minority homeownership rate to 50 percent in 2003.
- **Justice:** The Budget supports a six-month standard for processing all immigration applications. The Immigration and Naturalization Service will streamline and redesign its entire process, improving efficiency to reach this target. This will be done with a clear focus on thorough and timely screening of all applicants to ensure security. Justice has also set targets for immigration enforcement, prison crowding, and detention cost and quality.
- **Social Security Administration:** SSA has targeted an increase in retirement claims processed within 14 days from 84 percent in 2001 to 87 percent by 2003, an increase in customer initiated services available electronically from 21 percent to 40 percent; and an increase in callers access to SSA's 800 number within five minutes of their first attempt from 92 percent in 2001 to 94 percent in 2003.
- **Transportation:** DoT manages programs to improve safety in all modes. They have set targets to reduce the number of serious airport runway incursions from the 52 last year. The Department also hopes to reduce highway fatalities and injuries by increasing seat belt usage to 90 percent by 2005, and reducing alcohol-related fatalities to 11,000 by 2005.
- **USAID:** The Budget increases funding for global efforts to combat HIV/AIDS. A rapid scaling up of the program will focus on four countries (Cambodia, Kenya, Uganda, and Zambia) to reduce HIV prevalence in young adults by 30 percent, increase the proportion of infected, pregnant women getting antiretrovirals to prevent mother-to-child transmission to 7 percent, and increase the percentage of orphans receiving community services to 12 percent.

Adding Incentives to Enhance Program Effectiveness

Even effective programs can further enhance their results by adding incentives for grantees, contractors, and employees. For less effective programs, this could

provide a crucial boost to the search for innovation, efficiency, and new strategies.

- **Agriculture:** The Food Stamp quality control system measures how accurately States determine Food Stamp eligibility and calculate benefits. While the system is necessary to ensure program integrity, the current system's sole focus on payment accuracy does not recognize State efforts to achieve other important program goals, such as promoting access among working households. As part of Food Stamp reauthorization, the President proposes rigorous, but fair, reforms to the quality control system and performance bonuses for payment accuracy and customer service.
- **Commerce:** The Administration will propose that reauthorization of the principal legislation governing marine fisheries conservation enable the use of transferable fishing quotas in appropriate circumstances. This strategy can improve economic incentives for fishing investment and activity, which help both profitability and environmental sustainability. Currently, 20 percent of major marine fish stocks are over fished and another large fraction has unknown population status.
- **Education:** Vocational Rehabilitation State Grants are already rated effective, but States vary widely. As part of the initiative to integrate performance measures and budget decisions, companion Incentive Grants will be allocated to States based on their performance in helping individuals with disabilities obtain competitive employment.
- **Energy:** The Power Marketing Administrations provide an unusual example of improved incentives. PMAs receive their power from hydroelectric dams operated by the Corps of Engineers and the Bureau of Reclamation. In 2003, three additional PMAs will join Bonneville Power Administration in directly paying the Corps' operating and maintenance expenses, permitting the PMAs to negotiate directly with the Corps over their maintenance and upgrades.
- **Health and Human Services:** The effective Temporary Assistance for Needy Families (TANF) program began in 1996. TANF includes a system of high performance bonuses to reward States that have excelled in a variety of areas, including employment outcomes and continued access to benefits. The bonus to reward States with a reduction in out-of-wedlock births is less effective and so is being eliminated, with the funds redirected to develop new approaches to reduce illegitimacy and promote family formation.
- **Labor:** The Federal Employees' Compensation Act will charge agencies for the full cost of FECA administration as well as workers' benefits, and will implement a number of reforms to strengthen program integrity, discourage frivolous claims, and promote benefit equity.

- **State:** OMB and the State Department are coordinating an effort to right size the government's overseas presence. Information is being developed on how many employees from which agencies are stationed overseas and what they are doing. OMB and the State Department are developing a proposal whereby the many agencies that the State Department hosts will be charged for the full cost of the space and services that they use, providing a new incentive to balance cost against the benefit of overseas presence.
- **Treasury:** The United States proposes to negotiate a significant increase in the level of assistance provided to the poorest countries as grants rather than loans. The U.S. will focus this aid on countries with sound policy environments and demonstrated performance, and on operations that raise productivity. The institutions which distribute the aid will be asked to develop reliable performance and output indicators. The U.S. will increase its contributions in 2004 and 2005 conditional on specific actions and the achievement of results.

Improving Efficiency in Programs and Support Services

If the Federal role is appropriate and the program is effective or undergoing reform, then attention turns to the most efficient way to produce outputs. This is more difficult than in the private sector, where market price summarizes the value of the timeliness, accuracy, quality, and other characteristics of outputs. But attention to efficiency can result in the public getting more government services at the same or less cost.

- **Agriculture:** The Farm Service Agency and the Natural Resources Conservation Agency will work to reduce the reporting burden of the farmers they serve by 10 percent, and to increase the technical assistance to priority locations and the eligibility determinations they provide, while reducing cost.
- **Agriculture:** Rural Development has had considerable success centralizing loan servicing through a single, national office and information system. The Budget proposes that the Farm Service Agency emulate that success by establishing a service center to centralize farm loan servicing.
- **Defense and Veterans Affairs:** To increase the cost-effectiveness of providing medical care, the Department of Defense and the Department of Veterans Affairs will begin to coordinate with each other. They will share information to speed delivery of health services and ensure the safety of veterans who get care from both DoD and VA. They will also share resources instead of constructing new facilities, purchase supplies together, and coordinate patient transportation.
- **Education:** The Department of Education will reform the process of collecting Federal elementary and secondary education information from States in order to reduce administrative burden, maxi-

mize the usefulness of data, and improve accountability for results. This reform will permit staff to focus on results, thereby releasing the Department from a culture of compliance and shifting to a culture of accountability.

- **Education:** The Department of Education's costs for administering student financial assistance programs will be consolidated in a single discretionary account. Requests will be tied to unit cost targets for major tasks, such as applications processing, loan origination, and loan servicing, and to annual estimates of participation in various programs. These changes will enable the Department to measure its progress in meeting productivity and cost-efficiency goals.
- **Health and Human Services:** HHS is a many-layered bureaucracy with 40 Human Resources offices competing for recruits, more than 50 Public Affairs offices, and more than 20 Legislative Affairs offices. These will be consolidated into four Human Resources offices and one each for Public Affairs and Legislative Affairs. Three building maintenance and construction offices will be consolidated into one this year, and two more will be folded in next year, in order to concentrate

expertise and set priorities for capital projects across the Department.

- **Justice:** To use detention space efficiently, the Department of Justice will create a National Clearinghouse for Detention Space; State, local, and private providers will electronically post vacancies, rates, services, and other data. Justice will also explore purchasing private prisons.
- **Labor:** DoL is providing focused compliance assistance to help employers prevent labor law violations or correct them voluntarily. Efforts include making the rules more understandable, posting them on the Web, providing on-site consultations, and developing interactive electronic tools to help employers and others understand occupational safety and health regulations.

These examples show that there are Federal programs with documented effectiveness. These programs attract support in the President's Budget. They show that making decisions based even on today's rough performance measures can improve results—by allocating resources to more effective programs, stimulating program reforms, providing constructive incentives, and cultivating good program management. The integration of performance measures in the budget process encourages their use in making decisions that improve results.

FOUNDATION FOR RESULTS

Measurement leads to improvement, but it is hard to find good measures in the Federal government. For instance, currently many program managers cannot get a consistent, full measure of the costs of their programs from agency budget systems. Frequently they do not actively participate in developing performance measures for the performance plans required under the Government Performance and Results Act (GPRA). The goal of the Integration Initiative is to give program managers better information on costs, involve them in a process of setting goals that are commensurate with the resources requested, and then hold them accountable for results.

In the same vein, while some agencies have made good progress in performance reporting under GPRA, a lot more needs to be done. Even information about the relationship of existing performance measures to the budget costs for specific programs is frequently not available for decision-makers and the public. This Administration has devoted substantial time and effort over the past year to integrating goals and costs, including making major changes in the budget volume. Notwithstanding this effort, it continues to be difficult to systematically assess either the effectiveness of programs, or their relative efficiency when compared to like activities in other areas of government and the private sector.

This lack of full, consistent information is the result of long standing barriers in agency organizations and reporting systems, some of which are built into law.

To just begin to correct these deficiencies, the following steps are needed:

- The government's program managers must participate in the development of broad objectives and annual performance goals, and link those objectives and goals to an annual budget request.
- Agency reporting systems must be able to report on these goals, objectives, and costs in an integrated information system that can be aggregated into the President's Budget request and the agency budget justification that is transmitted to the Congress. Agency reporting systems must also provide acceptable after-the-fact evaluation and financial information on how well goals and costs have been achieved.

Making results the focus of the budget requires three significant changes. First, planning and evaluation—both oriented toward outcomes—must be thoroughly integrated into the budget process and documents. Second, the alignment of budget accounts—and especially their subdivision into “program activities”—should be reviewed so that the budget can readily relate resources used to the results produced, and so that good management is supported. This can be done separately for each agency. Third, accounts and activities should be charged consistently for the full annual cost of the resources used. This requires legislation.

In October, the Administration transmitted legislation to the Congress to charge the employer's share of the full accruing cost of retirement benefits to Federal employers. A companion bill to complete full charg-

ing for other resources used to produce outputs is being developed for transmittal following this Budget. Together, these changes are important steps toward a more results-oriented government.

The broad objectives of the Integration Initiative are clear enough, but, as with performance measurement in general, translating these objectives into specific goals and making the changes necessary to meet the goals is much harder and takes a long time. Many program managers, budget officers, performance measurement staff, and other government officials are struggling with this translation.

Integrating the Process

The first step in infusing planning and evaluation into budgeting is to produce greater collaboration. Some agencies report that these functions are already carried out by “the same” staff, and others are considering mergers. So far, the results of collaboration are usually more evident at the bureau than at the departmental level. Planning is more likely to precede budgeting at bureaus, and a crosswalk between performance goals and budget cost is often provided.

The Environmental Protection Agency is an example of an agency that has made substantial progress. It has an integrated staff to create the budget, set output targets, and evaluate implementation. Another useful practice is followed by Health and Human Services, which holds a department-level joint plan and budget review for each of its operating divisions to prepare for the Secretary’s budget submission to OMB.

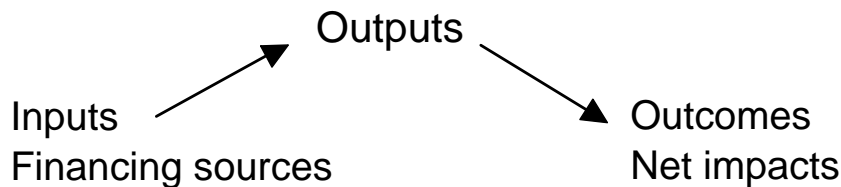
The second step is to make a serious commitment to outcomes—and to evaluation of relevant programs to understand how outcomes can be improved. A results-oriented budget starts from the agency’s strategic plan and its priorities. What outcomes will the agency espouse? How do its programs and activities help to achieve each outcome? Targeting an outcome, which the agency may influence but cannot control, seems risky. Yet without a serious commitment to outcomes, the agency’s programs may be efficient—but only accidentally will they be effective. Moreover, agencies without

this commitment are likely to have so many “performance measures” that few capture attention, get agency priority, or aggregate into results that the public cares about. Below are two examples of outcomes related to agency outputs. Note in the first example how an outcome—highway safety—may be produced by the outputs of several different agency programs and activities taken together.

- **Transportation.** To reduce highway fatality and injury rates, DOT will test automobiles to ensure compliance with safety standards; promulgate new or revised safety standards in several areas; invest in infrastructure improvements to reduce conditions or factors most associated with highway fatalities, such as single vehicle run-off-the-road crashes (which cause 38 percent of all deaths); and increase research into how the growing levels of driver distractions may increase accident rates.
- **Veterans Affairs.** To improve the overall health of veterans through high-quality, safe, and reliable health services (an outcome), VA has sharply increased its score on the Care Index (a measure of the degree to which VA follows nationally recognized guidelines for the treatment and care of patients with one or more of five major ailments) and on the Prevention Index (a measure of the degree to which VA follows nationally recognized prevention and early detection recommendations for eight diseases or health-risk factors).

Finally, a single streamlined, integrated plan-and-budget document should eventually be produced. So far, agencies have included budget amounts in their annual performance plan, first at an aggregate level and then in more detail. They have also included performance measures in their budget justifications, sometimes linked with program resources. Plans are relatively streamlined; budgets rarely are—not even in the sense of a streamlined overview with supplementary volumes. The Department of Labor and some other agencies are working toward a single integrated document. But few have learned a lesson from great chefs: “reductions” take more time, but they have more flavor!

Chart 1-1. Linking Resources with Results



- Program managers with authority over budgetary resources and staff offices are charged for the full annual cost of resources used and are responsible for efficient production of related outputs.
- Evaluation determines which outputs with which characteristics do most to improve the desired outcomes. Several programs may influence a single outcome.

Improving Alignment

Account and activity alignment should eventually fit the nature of each agency and bureau. Alignment needs to be considered with care. Consideration might begin with the question: What general principles for alignment contribute to creation of a results-focused budget?

Attention naturally turns to programs for the public that carry out the agency's mission. The agency's Strategic Plan, which is based on its authorizing legislation and involves wide consultation, is a potential starting point for identifying strategic goals and the outcomes that the agency seeks to improve. If the agency's perspective or environment have changed enough to affect its strategic goals (e.g., the Department of Justice after September 11th), they need to be brought up to date. The agency's main goals could be listed, along with the outcomes that measure success in achieving each. This could provide an organizing framework for the integrated plan and budget document.

The traditional—indeed Constitutional—purpose of the budget accounts is to control budgetary resources. That emphasis will continue, and no changes in budget concepts or total budget outlays are proposed as part of the Budget and Performance Integration Initiative. But the account structure needs review to ensure that it supports, or at least does not hinder, good management. From that perspective, all of the resources used by a bureau or other organization should be financed

from one or more budget accounts associated with it. At an aggregate level, resources would be managed by those accountable for achieving results.

Bureaus are clearly visible in the budget account structure of almost all Departments. Many accounts finance an entire bureau or office. Where there are more accounts, there is often a good managerial reason: a major program may have an account of its own; large mandatory transfers or grants may be in a separate account from administration and other complementary discretionary activities; if the bureau conducts programs and activities for very different major purposes, separate accounts may support better decisions. But multiple small accounts for similar purposes are usually unnecessary. And multiple accounts for different inputs or different activities leading to the same output or outcome may inhibit a manager striving for the best results. Some account consolidation might be useful.

The "program activity" sections that subdivide budget accounts offer an opportunity to improve linkage between resources and results. In accounts that finance provision of goods, services, grants, transfers, credit, insurance, or regulation for the public, program activities could align the resources used with the results achieved—usually an output for the public, such as loans made—with related performance measures that influence desired outcomes, such as the percent of loans made to first-time homeowners and the percent that

remain in payment status. This is sometimes current practice. But in other cases, these subdivisions may show inputs, some-but-not-all of the funding for an output, or an intermediate process that contributes to sev-

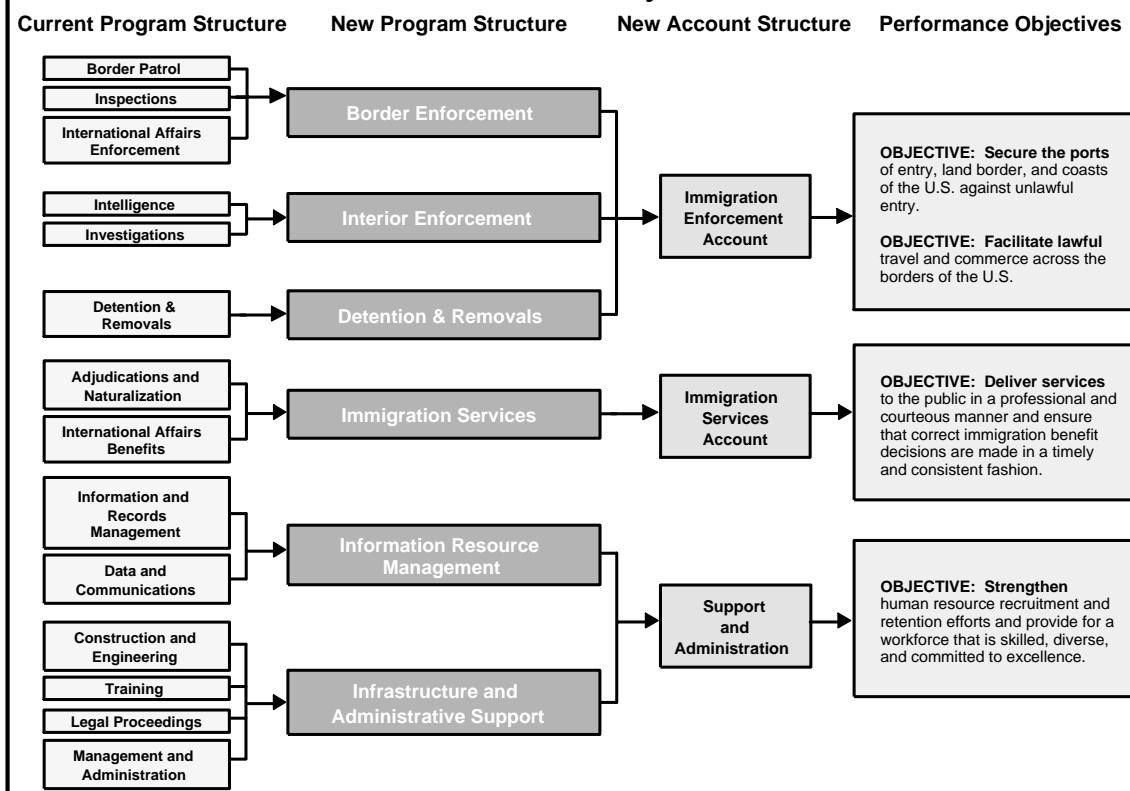
eral outputs. Such practices make it difficult to show the full annual cost of resources used to achieve specific results. They also splinter responsibility for achieving results that Americans value.

Immigration and Naturalization Service Program and Account Restructuring

In 2003, the Administration is proposing a realignment of the Immigration and Naturalization Service's (INS's) account structure. In the past, INS had three accounts: salaries and expenses, construction, and immigration support. A person looking at the INS accounts could not determine how much money was spent on immigration enforcement or immigration services. Even looking at various fee accounts, one could not see how much of the money collected from application fees went to processing the application versus enforcing immigration law. The new structure provides the full picture of how much money collected from application fees went to processing the application versus enforcing immigration law. The new structure provides the full picture of how much money is spent to fulfill the agency's dual missions of enforcement and services.

This proposal realigns the INS budget and account structure with the Department of Justice's and INS's Strategic Plan objectives, making it easier to track resources with results. It not only changes the account structure but also collapses the current program structure from 13 different programs to six programs that directly link to performance objectives. It organizes similar enforcement actions together and clearly separates immigration services and support operations. The support and administration account is temporary, capturing the overhead and support costs that could not be easily spread in the first year. INS plans to spread these costs in the 2004 budget. This will complete the realignment of funding to allow for linking funding with performance goals—so the public knows what it is getting for its money.

Chart 1-2. INS Program & Account Structure Linked to Performance Objectives



Thoughtful long-term reforms are needed in budgetary structure to manage for results. The Federal Aviation Administration is improving its budget accounts for capital and research by aligning funds under performance outcome goals. The agency is also streamlining these accounts to increase managerial flexibility to achieve performance outcomes. A more extensive example of an agency working on this problem is the Immigration and Naturalization Service. The presentation on the previous page shows their prior account structure, how they transformed it, and how it lines up with INS's performance objectives.

Charging Full Annual Budgetary Cost

To show the full annual budgetary cost consistently across all programs requires more than improving account and activity alignment. It also requires providing budget authority to cover the resources used for each program and oversight account, and charging all accounts for the full annual cost of using resources. Currently this is not systematically done.

- Civilian retiree health benefits have all been paid centrally for the whole government; military health benefits have been paid centrally by DoD and the small uniformed services. Costs are not shown when the benefits are earned; only when they are paid.
- Pensions for new civilian employees and for military employees were reformed in the mid-1980s, with employers paying their share of the accruing cost. But costs for employees hired earlier under the Civil Service Retirement System are only partly charged, and several small systems are pay-as-you-go, which creates an uneven effect across programs.
- Support goods and services are often paid centrally by agencies or provided to programs at less than full cost. There are indications that programs use different amounts and kinds of support in these circumstances than when they pay full cost. In other instances, agencies may allocate cost to the programs, leaving managers feeling burdened.
- Capital costs are most problematic. From the program manager's perspective, they may be zero if financed centrally, some share of acquisition cost if that is allocated, the rental value if office space is rented from GSA, or a substantial bite out of their budget for a rare capital acquisition.

In sum, program costs are often lower than annual operating costs—by widely varying amounts—and sometimes higher. The Budget and Performance Integration Initiative will improve on this and begin to create more complete and uniform measures of annual budgetary cost across the government. That will begin to permit the fair comparison of the cost of one program with another.

Two complementary legislative proposals—one already transmitted to the Congress and the other under development—would apply “best practice” consistently

to show a more complete measure of budgetary cost where and when resources are used.

- To show resources where they are used, the second proposal would include a straightforward but powerful requirement: the full annual budgetary cost of resources used by programs shall be charged to the budget account or accounts that fund the program. More than one program might be funded by a single account so long as the amounts used are separately distinguished. These provisions would be deliberately general, leaving how they would be applied to case-by-case decisions on alignment.
- To show support services where they are used, the second proposal would create intra-governmental support revolving funds (ISRFs) from working capital, franchise, and other support revolving funds. Any support goods and services provided to more than one bureau would move into an existing fund or a newly created one. Like all other accounts, ISRFs would be charged for the resources they use and would charge programs and other customers enough to operate on a self-sustaining basis.

Three other provisions of legislation would use pairs of budget accounts to change when costs are shown in the program accounts without changing the timing for the budget totals. These cover all major cases where resources are used long before or long after they are paid for.

- Pensions and retiree health benefits are earned as Federal employees work; they are paid much later, after the employees retire. The legislation already transmitted would require program and other employer accounts to pay the employer share of the accruing cost of these benefits to retiree benefit accounts, where they are offsetting collections. These accounts would pay the benefits when they come due.
- Similarly, programs that generate hazardous substances would be required to pay the accruing cost to clean up contaminated assets at the end of their useful life. These payments would go to funds responsible for the cleanup.
- In contrast, capital assets are bought before they are used. In this case, an agency Capital Acquisition Fund (CAF) would be created. Following good budget practice, the CAF would request budget authority (BA) up front to acquire assets that are included in the budget, and outlays would be recorded when payment was made. However, this BA would be in the form of borrowing from Treasury authority. The CAF would then borrow for the period of the asset's useful life; collect annual capital user charges in proportion to asset use, and make the mortgage payments to Treasury.

The General Accounting Office supported these concepts for budgeting in the United States in a recent report, *Accrual Budgeting: Experiences of Other Nations and Implications for the United States*. (February 2000).

Full Funding for Federal Retiree Costs. To make quick progress on these practices, the Administration split the required legislation into two parts. In October, the first bill—"Budgeting and Managing for Results: Full Funding of Retiree Costs Act of 2001"—was transmitted to Congress as Title II of the Managerial Flexibility Act of 2001.

The proposal charges to salary and expense accounts in all Federal agencies—most of which are funded by discretionary appropriations—the employer's share of the full annual accruing cost of retirement benefits above and beyond the amounts that are charged now. The bill requires charges for:

- the full accruing cost of the Civil Service Retirement System and the parallel Foreign Service and CIA pensions,
- retired pay for the small uniformed services (Coast Guard, Public Health Service, and NOAA),
- retiree health benefits for civilian employees in the Federal Employee Health Benefit Program, and
- retiree health benefits for the seven uniformed services. For the latter, accrual of health benefits for those 65 and over will start in 2003 under existing law, and accrual of benefits for younger retirees is proposed to start in 2004.

Existing liabilities are amortized by mandatory payments from the general fund, and benefit payments are mandatory.

This component of cost was proposed first because it could be implemented largely by changing the amounts paid from and to existing accounts. These costs are displayed by account in the 2003 Budget for 2003 and beyond, with comparable estimates published for 2001 and 2002.

The bill does not change total budget outlays or the surplus/deficit; it shifts costs from central mandatory accounts to increase the affected discretionary accounts on the civilian side by \$9.2 billion. The additional discretionary amounts were treated as an adjustment in this Budget.

Thus, the Budget requests sufficient funding by account for this conceptual change, except for programs that are funded by user fees. Under OMB Circular A-25, the costs of the latter programs are expected to be covered by their fees. The adjustment for accounts producing support goods and services is made in their customers' budget accounts.

This legislation would fully fund the employer share of all Federal pensions, retired pay, and retiree health benefits by agency payments to the retiree benefit funds each year as they are earned by employees. It would amortize past unfunded liabilities on a regular schedule by payments from Treasury to the retiree benefit funds.

The legislative language requires the appropriate amounts to be paid out of all salary and expense appropriations, just as they are now for the Federal Employee Retirement System (FERS) and the Military Retirement System (MRS).

These charging practices would go a long way to close the gap between current budgetary cost and uniform full operating cost so that cost and results can be compared with each other and across programs.

The bill would not change the government cost that would be compared with private offers in a public private competition. These costs are already included in the OMB Circular A-76 comparison. But it moves toward the possibility of fair competition without the current burdensome process.

Full Budgetary Cost and Performance Integration. As discussed above, the Administration is developing a second proposal to charge uniformly for other resources where and when they are used. It is intended for transmission to Congress after this Budget. Implementation would start in the fiscal year 2004 Budget, but with additional implementation in future years. This proposal covers the 24 CFO Act agencies, except that the Director of OMB may extend the support goods and services provisions to other agencies.

While still under review, this proposal's key goal is to facilitate the full annual budgetary cost of resources used by programs being charged to the budget account or accounts that fund the program. More than one program may be funded by a single account so long as the amounts used are separately distinguished. How this is worked out in each agency—and how closely it hews to the spirit of aligning costs with outputs and outcomes—will determine where the costs defined in the other provisions will be charged. To retain the current degree of flexibility to deal with changing circumstances, the proposal will include limited transfer authority.

None of the budgetary changes in this proposal will affect the "bottom line" of the budget as a whole, or the basic budgetary concepts of budget authority, obligations, and outlays. They do increase the amount of discretionary budget authority that must be appropriated to capture the full cost of programs. The effect of this will be that programs that produce outputs for the public will recognize discretionary spending in the budget at the time when they incur costs.

Therefore, for each program, the budget account would show the total budgetary resources used to pay annual operating cost. Comparison of resources and results will be systematic when allocating resources; and managers will have timely feedback and better resource control with which to achieve better results.

MANAGING FOR RESULTS

What you measure is what you get. The greatest initial impact from integrating performance and budgeting is that we will begin to get better results for

each budget dollar. In the slightly longer run, managing for results will continually improve program outcomes. *The President's Management Agenda* launched this ef-

fort last August. The Agenda includes five government-wide initiatives that are intended to work together as a mutually reinforcing set of reforms. In addition to Budget and Performance Integration, they are Strategic Management of Human Capital; Competitive Sourcing; Expanding Electronic Government; and Improving Financial Performance.

The Strategic Management of Human Capital Initiative will align human resources with programs and their outputs, so that real as well as budgetary resources will be focused on producing results. The Competitive Sourcing Initiative will give program managers more choice in the character and cost of the inputs they buy with the budgetary resources they control. The Expanding Electronic Government Initiative will help programs to coordinate and deliver services. And the Improved Financial Performance Initiative will integrate financial and performance information that, together with Budget and Performance Integration, will provide timely, analytical feedback to managers. These Initiatives place more authority and accountability for outputs at the operating level, use working groups and intermediate levels of management to coordinate pro-

grams to influence outcomes effectively, and focus top management on policy development and oversight.

The basic idea is to align authority, staff, and all resources used with specific bureaus and programs, to provide flexibility in the use of those resources, and to hold managers and staff accountable—with rewards when successful—for achieving agreed-upon results. Following the spirit of accountability, this Budget is presented by Agency rather than by cross-cutting functions.

These five government-wide Presidential initiatives were selected because in each area the Federal Government is operating below potential, yet there is also a clear path to improvement with a major pay-off at the end. As a goal post, each of the initiatives included standards setting forth the characteristics that would define the success to be achieved over the next three years. OMB is working with agencies to customize the progress that each agency should make this year to achieve full success within three years. Agencies will earn “green lights” on progress for each quarter in which they meet the milestones along their agreed pathway to success.

Chart 1-3. Moving Toward Results-Oriented Government

Results orientation will be infused into every aspect of government:

Budgeting -- results, targets, and structure

Managing -- in the spotlight

Staffing -- align and empower staff, reward results

Acquisition -- competitive, performance-based

IT -- integrated, timely, delivering service

Reporting -- accurate, timely, and integrated

Strategic Management of Human Capital

A growing portion of the Federal workforce will become eligible to retire over the next decade. Good human resource management is needed to ensure that people with the necessary skills are hired, trained, and retained to provide public services. Human resources, as well as budgetary resources, need to be aligned with programs and activities that produce results. Aligned managers should be delegated the authority they need to get the job done, including more flexibility to hire and manage personnel, rather than hampered by excessive layers of review. The Integration and the Human Capital initiatives both link rewards to individual and group success in reaching performance goals. Below are examples of good practice.

- **Treasury** implemented knowledge management systems to help preserve and share the experience and institutional memory of retiring employees.
- The **Veterans Affairs** Healthcare Network for Upstate New York involves its employees in developing work unit “stretch” goals at least 10 percent higher than the consensus expectation for the amount of work that will be accomplished. Employees have a stake in their success through a “goal sharing” incentive program, where modest awards are based on reaching goals at the regional and unit level. Since the program began, the program has reduced cost per patient and improved customer service and satisfaction.
- The **General Services Administration’s** Public Buildings Service allocates regional office budgets based on nine performance measures. Targets are set for each measure, and a portion of the Performance Excellence Pool goes to regions for each goal they exceed. Organizational and individual performance has improved across the measures, with lower costs and better efficiency, effectiveness, and customer satisfaction.

Competitive Sourcing

The President’s Management Agenda includes an initiative to acquire an increasing proportion of commercial goods and services through competition among and between public and private sources. The process, as defined in OMB Circular No. A-76, relies on a performance-oriented statement of work and a comparison of the full costs to the taxpayer for each source. Last March, OMB set a target for agencies to compete or convert to contract not less than 5 percent of their FAIR Act inventories of commercial work performed by Federal employees in 2002. Agencies were asked to compete an additional 10 percent of their FAIR Act inventory in 2003. The agencies will retain all of the savings achieved through Competitive Sourcing.

Innovation and efficiency are stimulated when agencies compete the acquisition of support goods and services from providers in their own agency, other agencies, or the private sector. Savings are generated which can be put to use in support of the agency’s mission. The Department of Defense has competed 218 competitions

since 1955, of which 57 percent were retained in-house, and 43 percent converted to contract. When retained in-house, the average savings were 34 percent.

However, OMB Circular A-76 is a cumbersome and complicated process. It requires developing a performance-based contract, conducting a management study to design a most-efficient-organization for the in-house bidders, and making an elaborate cost comparison. The process needs to be reformed to allow program managers to be free to acquire the support goods and services that best meet their needs.

Expanding Electronic Government

E-government can improve the coordination, efficiency, and effectiveness of delivering information and services to the public. These projects may bring together programs producing different outputs toward common outcomes, and help them to deliver services from the customer’s perspective. In order to make the government truly “citizen-centered,” agencies will have to work together around the needs of citizens and businesses—not agency boundaries. Citizen-centered government will use the Internet to give citizens the ability to go online and interact with their government. Below are some interesting examples.

- The Department of Commerce is using the Internet to serve businesses interested in international trade and minority contracting opportunities. Census uses e-government for its economic surveys of firms, and will use it more for the 2010 census of population.
- The Department of Labor’s Occupational Safety and Health Administration accepts health and safety complaints over the Internet. In addition, individuals can use the Internet to discover lost pensions, and a pilot project allows people to calculate their approximate retirement benefits online.
- The National Science Foundation was the first agency to perform all of its critical interactions with its proposal applicants through the web. Over 99 percent of the proposals the agency receives are submitted electronically.
- The Social Security Administration is rapidly expanding online customer service options. These include making retirement claims, receiving Medicare replacement cards, checking account status online, getting access to change one’s address and telephone number, and making direct deposits.

Improving Financial Management

Financial management is a natural complement to budgeting. Better account and activity alignment with performance is needed; resources should be charged where they are used. This congruence would facilitate accounting, and the emphasis on performance would provide incentives for, as well as facilitate, cost accounting. Performance, budgeting, and accounting information potentially could be entered using standard analytical software at the program and activity level, where

it would be familiar and used as timely feedback, making it likely to be accurate. All entries should be fully coded to the Standard General Ledger. The modules as a whole could then be uploaded and consolidated.

- **Transportation** is implementing a new Department-wide financial management system that is geared towards capturing transactions at the source, automating the matching of expenditures to the obligating document, and obtaining electronic approvals. By capturing transactions at the source, this process reduces the likelihood of erroneous payments and posting the charges to the wrong contract. All organizations in DOT are working to convert to the new system by the end of calendar year 2002.
- The **Treasury** Franchise Fund consists of eleven "business activities," each with a separate account established to facilitate financial reporting. Although the audited financial statements of the Fund are presented on a consolidated basis, its financial system generates individual financial statements for each business activity. Revenue and expense data are recorded and reported by business line. Direct and indirect costs are identified by each business activity and reported internally on financial reports.
- The **Social Security Administration** included a comprehensive footnote disclosure in its Accountability Report that described the method they use to classify operating expenses by strategic goal. SSA aligns its strategic goals with its request for new budget authority as part of its annual budget

request. They applied the same method to allocate primary administrative expenses to each strategic goal and reconciled that to the operating costs reported on the Statement of Net Cost.

- The **Department of Education** is using activity-based costing in its student financial assistance (SFA) programs to improve efficiency. SFA has worked with managers to define program and business activities, assign cost, and map the activities. A user-friendly reporting tool provides managers with on-line multidimensional views of the results. Quarterly management reports are provided to managers showing the cost of their business processes and providing insight into the drivers of those costs. Managers are being assigned cost reduction targets, which this system and benchmarking with private industry and other agencies will help them to meet.
- The **Environmental Protection Agency** provides integrated financial and programmatic data to the agency's managers to support decision-making based on costs. For example, EPA is tracking the cost for all major IT projects by phase. Agency cost accounting for the Superfund program has resulted in over \$2.8 billion in cost recoveries. And the agency's accounting structure has been redesigned to provide the costs of achieving the goals, objectives, and sub-objectives embodied in their Strategic Plan and budget.

All five of the President's Initiatives thus contribute to the performance orientation and effectiveness of the Federal Government.